

Where to find the money? Replacement income after permanent disability.

By Craig Gillespie

An accident causing a permanent disability is, without question, a profound life changing experience for the injured individual and his or her family. If the resulting disability is severe enough that the individual can no longer work, the prospect of no future income becomes a major concern. There are a variety of means through which a disabled individual can obtain some form of income replacement.

The Alberta government provides income support to persons with permanent disabilities through AISH - Assured Income for the Severely Handicapped. A severe handicap is one that prevents the person from earning an income through employment. To qualify for AISH, however, there are strict limitations on the amount of assets an applicant can own and the amount of income an applicant can receive before benefits are reduced. I will discuss these in more detail shortly.

Disability insurance is the next most obvious income replacement program for those employees who have disability insurance coverage through group plans, or if self-employed, through their own privately purchased disability insurance policy. The purpose of disability insurance is to protect against the loss of income resulting from a permanent disability. Disability insurance provides income replacement benefits to workers who are “totally disabled” as defined in the policy. The key is whether the policy protects against an inability to perform the duties of one’s own occupation, or any occupation. I will discuss these distinctions in turn.

For those individuals whose injury and subsequent disability were caused by the fault of a third party, as in a car accident or medical malpractice situation, a tort claim (a lawsuit) might lead to compensation in the form of damages. A typical damages award will include a claim of general damages for pain and suffering and loss of amenities of life, but it will also include damages for future loss of income.

The Assured Income for the Severely Handicapped program provides financial assistance in the form of a living allowance, supplementary assistance in the form of child benefits and personal benefits, and health related assistance in the form of health benefits to adults with disabilities.

The legislation defines severe handicap as follows:

“‘severe handicap’ means an impairment of mental or physical functioning or both that, in a director’s opinion after considering any relevant medical or psychological reports, causes substantial limitation in the person’s ability to earn a livelihood and is likely to continue to affect that person permanently because no remedial therapy is available that would materially improve the person’s ability to earn a livelihood.” (Section 1(I), *Assured Income for the Severely Handicapped Act*, S.A. 2006, c. A-45.1)

In other words, the disability must be permanent and must severely limit the ability to earn a living. The disability must be the main factor behind the inability to earn a living, not the person’s age, lack of education, or lack of available jobs. An applicant for AISH must also meet income and asset thresholds. To qualify, the applicant and his or her cohabiting partner must not own more than \$100,000 in non-exempt assets. Certain key assets are exempt, including a principal residence and a vehicle, and a second vehicle if it has been modified to accommodate the applicant’s disability. Clothing and basic household goods are also exempt from the asset calculation.

All AISH applicants must also apply for any other income benefits they are eligible to receive, such as Canada Pension Plan disability benefits. AISH applicants must also claim or collect the benefits of any assets they are entitled to receive.

AISH provides a maximum monthly living allowance of \$1050/month. This amount was increased by \$50 from the previous maximum of \$1000 on May 1, 2007. The actual monthly living allowance depends on each applicant’s income. New income rules, also brought into force

on May 1, are intended to simplify how earned income affects the monthly living allowance. In simple terms, each AISH recipient can earn a minimal base amount of income that is fully exempt. The amount of this exemption is different for recipients who are single, who are cohabiting with a partner, and for those who have dependent children. There is a further exemption for a percentage of any additional income earned. The remaining income reduces the AISH benefit for that month. AISH recipients are required to report changes in their income on a monthly, quarterly, or yearly basis, depending on how frequently their income changes.

AISH also provides a \$315 living allowance to qualified applicants who reside in a residential care facility, as well as an accommodation charge to assist with the cost of living in the facility.

For many of you, \$1,050 per month is not a sufficient living allowance or income replacement benefit. This explains why disability insurance is such a popular form of protection. Disability insurers know that we are all extremely dependent on our income stream. As such, most disability policies focus on disability that interferes with the capacity to work at an occupation and earn a living. Each disability policy has its own definition of total disability. In general, these policy definitions can be divided into two categories: “own occupation” policies and “any occupation” policies.

“Own occupation” policies cover the insured so long as he is rendered incapable of pursuing the occupation in which he was engaged at the time he became disabled. The assessment of disability focuses on whether the insured is able to perform substantially all of the duties of his occupation.

“Any occupation” policies provide benefits only where the insured is unable to engage in an occupation for which she is suited. The benefits provided by “any occupation” policies are much narrower than those provided by “own occupation” policies. The “any occupation” policy benefits end as soon as the insured has recovered enough to work at a suitable occupation or one for which she is reasonably fitted, regardless of whether she is able to do the type of work she is

accustomed to doing. The assessment of disability in this context involves a consideration of a number of variables, including the state of health and physical capabilities of the insured, and his or her education, training and experience, as well as the general suitability of the proposed alternative occupations.

It is up to the insured to show, usually through medical evidence, that they cannot work at his or her own or another occupation. The burden then shifts to the defendant insurer to identify jobs that are within the insured's capabilities and for which the insured has the proper education, training, or experience.

It is quite common for a disability insurance policy to provide "own occupation" coverage for two years, after which the policy definition of total disability changes to an "any occupation" type of definition. In spite of these reasonably narrow limits, however, the courts have decided that disability insurance policies should be interpreted "liberally", not "literally". Since the purpose of disability insurance is the protection of income from employment, the courts will not require an insured to take "just any job".

The alternate occupation or work must be similar in relation to income, status, regularity, and so on. An occupation for which the insured is "reasonably fitted" is one which is not inconsequential or trivial and which is similar in nature and remuneration to her usual occupation. Judges will not compel a person who is accustomed to heavy physical labour or outdoor work to adapt to clerical duties or other light work in an office or a store. Similarly, professionals, managers, business executives or other individuals involved in specialized line of work at a high level will not be forced to move to another line of work. Each case is decided on its facts. For example, these principles might not apply in the same way to a younger worker, who is less settled in his or her career.

The courts have also recognized that a person might meet the definition of total disability if they are hindered in the performance of their duties by pain, fatigue, or some other impediment. A

person can also meet the definition of totally disabled if a reasonable person, that mythical creature of the law, would recognize that he should refrain from certain activities and/or stop working to prolong his life or effect a cure for his illness.

As you can imagine, these definitions of total disability leave a lot of room for argument with disability insurers. Recently, the courts have started punishing insurers for these arguments. A disability insurance policy is understood to be a peace of mind contract. In paying premiums for a disability insurance policy, the insured expects that benefits will be paid if a disability strikes and leaves him without the ability to earn an income. The insurer has a duty to meet its contractual obligation, that is, to pay benefits to those persons entitled to them. When the insurance company wrongly denies these benefits and forces the insured to bring a lawsuit to gain the benefits to which he was entitled, the insured can claim damages not just for the benefits under the policy, but additional damages for the mental suffering and stress caused by the refusal. In *Fidler v. Sun Life Assurance Co. of Canada*, 2006 SCC 30, the Supreme Court of Canada approved the trial judge's award of \$20,000 in aggravated damages to compensate the insured for the insurance company's denial of her claim over a five year period. Aggravated damages are the courts' way of compensating an insured forced to litigate for the lost peace of mind.

In an earlier Supreme Court of Canada decision, *Whiten v. Pilot Insurance Co.*, 2002 SCC 18, the court approved a jury award of \$1 million punitive damages against an insurance company. Punitive damages are not designed to compensate; they are designed to punish. The purpose of punitive damages is retribution, deterrence, and denunciation. Punitive damages are meant to be the exception, rather than the rule. They are saved for high-handed, egregious, arbitrary or highly reprehensible misconduct that departs to a marked degree from ordinary standards of decent behaviour.

In *Whiten*, the insured lost her house in a fire. The insurance company denied her claim, alleging arson. The company pursued a deliberate course of conduct that was designed to force the

insured to make an unfair settlement for less than she was entitled. It continued this conduct for more than two years while the insured's financial situation became increasingly desperate. In the end, she had to spend \$320,000 in legal costs to collect the \$345,000 she was owed under the policy. The jury was so outraged by the insurance company's conduct that it awarded \$1 million in punitive damages. The Supreme Court of Canada found that this amount was at the high end of the acceptable range, but that it could be reasonably supported on the facts of this case.

In *Fidler*, by contrast, the Supreme Court of Canada concluded that the facts did not support a claim for punitive damages. Although the insurance company's actions in denying the insured's total disability claim in the face of supporting medical evidence were troubling, the company's actions were not so high-handed, malicious, egregious or highly reprehensible to warrant retribution, deterrence or denunciation.

The final means to get compensation for loss of income is through a tort claim - bringing a lawsuit against the person who caused the injury and subsequent disability. A plaintiff can claim compensation in the form of general damages and special damages. General damages include damages for pain and suffering and loss of amenities of life, as well as damages for past loss of income, meaning the loss of income between the injury and trial, and future loss of income, as well as estimated costs of future care, and so on. Special damages can include damages for specific costs incurred as a result of the disability such as medical prescriptions, treatments, adaptive aids, etc.

Although the eventual outcome of a lawsuit can be quite positive, financially at least, lawsuits present their own headaches. They often take a long time to finalize and there can be significant costs along the way. Although many personal injury lawyers will offer contingency fee agreements to their clients, which generally provide for payment only after the case settles or is successful at trial, there are numerous other costs that must be paid along the way. Filing fees for court documents, payments to medical witnesses and other experts, photocopying of medical records, and so on. These up front costs can be quite a burden on a disabled individual who is

already short on assets or income.

There is another problem: the risk of a costs order against an unsuccessful plaintiff. Costs are a reimbursement for the expense of bringing or defending an action. Typically costs follow the event. In simple terms, this means that the loser pays the winner's costs. The Rules of Court contain a schedule through which costs are calculated for each step of a lawsuit. Although costs do not necessarily reflect the true and complete cost of bringing an action, they are still a significant burden to the loser of a lawsuit. The likelihood of having to pay costs will depend on the strength of the claim. In any lawsuit, the prospect of having to pay costs creates a risk - a risk that is often used by defendants to force you to settle early.

Another tactic frequently used to frighten plaintiffs into early settlement is the formal offer to settle. The Rules of Court have created a process whereby either side can make a formal offer to settle the action before trial. If the other side rejects the offer, and then does not better the offer at trial, they will owe double costs from the date of the offer up to the end of the trial. For example, a defendant offers to settle the plaintiff's claim for \$50,000. The plaintiff refuses and the matter goes to trial. At trial, the plaintiff loses. The plaintiff now owes the defendant double costs for every part of the action taken between the offer to settle and the trial. Even if the plaintiff wins, but gets less than the amount offered, let's say \$40,000, then the plaintiff owes costs to the defendant from the offer to settle all the way through trial even though the winner doesn't usually pay costs.

The same rules apply in reverse, so the plaintiff has the option to play the same game. If the plaintiff makes a formal offer that the defendant refuses, and the plaintiff equals or betters that offer at trial, then the defendant is liable to pay the plaintiff double costs.

The Rules regarding double costs are meant to act as an incentive to early settlement.

Unfortunately, the profound financial consequences associated with these Rules are sometimes used as a stick to force early settlement where the plaintiff is afraid of the potential consequences

of proceeding in the face of a formal offer to settle.

The risks and financial problems just described apply to all litigation, whether it is an action against the person who hit you in a car accident or whether you are suing your disability insurance company for its denial of your disability claim.

The news is not all bad. Many plaintiffs are successful against insurance companies and against those who caused their injuries. A successful plaintiff will not only recover costs, but will win a damages award. The law requires that the court award damages as a lump sum, unless the parties agree otherwise. The trouble with a lump sum payment is that it leaves the plaintiff with the responsibility to manage and invest the funds to create a regular income stream for him or herself. Few plaintiffs are astute money managers, nor do they know how to find a suitable investment advisor. Furthermore, although the initial lump sum damages award is not taxable, the interest earned on the capital is taxable as investment income. To avoid some of these investment and taxation challenges, lawyers have come up with structured settlements.

A structured settlement is a voluntary agreement between the parties to the lawsuit whereby all or part of the damage award is paid out through periodic payments rather than through a lump sum. For example, there may be an initial lump sum payment to pay out the plaintiff's mortgage, cover the cost of renovations to the home for ramps, or an elevator, or a main floor bedroom, or to cover the cost of adaptive aids and equipment such as a wheelchair or a special van, and perhaps provide funds for a much needed holiday. The remainder of the funds would then be structured through periodic payments, with perhaps some additional lump sum payments to cover replacement adaptive aids, and so forth. The arrangements range from simple to sophisticated depending on the needs of the parties. There are specialized firms in business doing nothing other than preparing structured settlements.

One of the main advantages to structured settlements is that the periodic payments are not taxable, just as the one-time lump sum payment of a damages award is not taxable. Another

advantage is spendthrift protection. A structured settlement can protect a financially inexperienced plaintiff from losing a large portion of his settlement through inappropriate spending or vulnerability to pressure from family or friends. The settlement creates a guaranteed income stream for the disabled individual who needs this financial security. Structured settlements are a safe choice in that only federally registered life insurers can underwrite structured settlements.

According to an article in *Canadian Lawyer*, “the typical plaintiff seeking a structured settlement is a catastrophic victim, one who has future care needs and no prospect or limited prospects of income from employment or other sources during their lifetime.”¹

Structured settlements can also help a disabled individual retain their AISH benefits. In the case of a severe injury, a lump sum payment could put the AISH applicant over the \$100,000 asset threshold. A structured settlement could be crafted to meet the specific needs of an AISH recipient. For example, a lump sum payment could be provided to pay out the mortgage on the home, since the principal residence is an exempt asset. Similarly, a lump sum payment could provide for a modified vehicle, another exempt asset. The remainder of the settlement could be structured in such a way to limit the impact on any AISH entitlement. The periodic payments will count as income in the month they are received. Depending on the amount of the payment, they might reduce the AISH benefits in the month they are received. They would not, however, impact overall AISH eligibility.

The main critique of structured settlements is that they do not provide the same rate of return that might be obtained through aggressive investment of a lump sum. In each case, the decision as to whether a structured settlement is worthwhile will depend on the specific needs and circumstances of the individual plaintiff. The earlier a structured settlement is considered, the better, as it can then be best planned to suit the plaintiff’s needs.

¹Julius Melnitzer, “Structured settlements: take the long way home” *Canadian Lawyer* (June 2005) 29:6, at 33.

While it may seem that all is lost after someone suffers a disabling injury, there are in fact a number of ways in which the individual can recover, at least financially. Between a tort claims, disability insurance, or the government-sponsored support provided through AISH, disabled individuals who are no longer able to earn an income can find some form of income protection.

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